

No. 34863

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

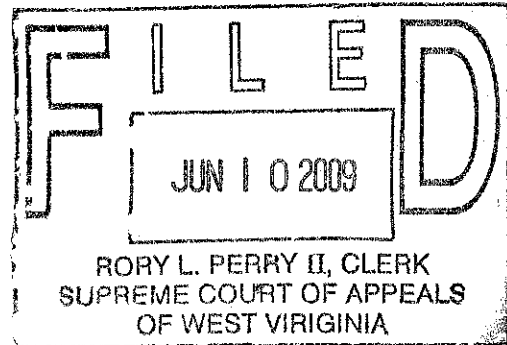
**OTTIE ADKINS, ASSESSOR
AND THE COUNTY COMMISSION
OF CABELL COUNTY,**

Respondents Below/Petitioners,

v.

PINE HAVEN LIMITED PARTNERSHIP, et al.,

Petitioners Below/Respondents.



**Brief of Appellees Pine Haven Limited Partnership,
The Hamlets Limited Partnership, and
The Parks Limited Partnership (Parkview LP)**

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I. Introduction

The issue before this Court is an important one. As a part of President Truman's "Fair Deal" in 1949, Congress established the public policy of striving to provide "a decent home in a suitable living environment for every American family"¹. In the National Affordable Housing Act of 1990², Congress affirmed "the national goal that every American family be able to afford a decent home in a suitable environment".³

Since 1987, the principal mechanism established by Congress for supporting the production of new and rehabilitated rental housing for low income households has been the Low Income Housing Tax Credit (LIHTC) program. Under this program, the federal government

¹ The Housing Act of 1949 [42 U.S.C. 1441 *et seq.*].

² 42 U.S.C. § 12701 *et seq.*

³ 42 U.S.C. § 12701.

spends approximately \$5 billion annually⁴ and creates between 60,000 and 90,000 new units of affordable housing each year.⁵

Pine Haven Limited Partnership (“Pine Haven”), The Hamlets Limited Partnership (“The Hamlets”), and The Parks Limited Partnership (Parkview LP) (“The Parks”), the Appellees herein, own and operate multi-unit apartment buildings that provide low-income housing in Cabell County, West Virginia. Finding of Fact No. 1, Order Granting Summary Judgment at 2. All three projects were developed under the LIHTC program through the West Virginia Housing Development Fund. Finding of Fact No. 2, Order Granting Summary Judgment at 2. The Circuit Court below found that “the intent of this program is to make it economically feasible for private developers and investors to develop affordable housing to meet the demonstrated demand for quality housing at reduced rents for senior citizens and the working poor”. Finding of Fact No. 3, Order Granting Summary Judgment at 2-3.

Congress elected to utilize the federal tax system as the vehicle to further the goal of providing affordable housing, but, as commentators have recognized, state or local *ad valorem* property tax systems can undermine that goal. To make housing affordable, the LIHTC program requires owners to severely limit the rent they can charge. When income is limited, excessive operating expenses can cause potential projects to be deemed unfeasible⁶ or can cause existing

⁴ See Climaco, Finkel, Nolan, and Rich, *Updating the Low Income Housing Tax Credit (LIHTC) Database: Projects Placed in Service through 2002* (2004) at 2; available at <http://www.huduser.org/Publications/pdf/updtlihtc.pdf>; last viewed February 25, 2009.

⁵ Leviner, *Affordable Housing and the Role of the Low Income Housing Tax Credit Program: A Contemporary Assessment*, 57 Tax Law. 869 (2004).

⁶ See Penna, *Fairness in Valuation of Low-Income Housing Tax Credit Properties: An Argument for Tax Exemption*, 11 Journal of Affordable Housing and Community Development Law 53 (2001) at 54 (“Because the typical operating budget of an LIHTC property includes little or no cash flow and rental rates are restricted by statute, nonprofit developers must sometimes abandon projects before they get off the drawing board”); McNeely, *Improving Low Income Housing: Eliminating the Conflict between Property Taxes and the LIHTC Program*, 15 Journal of Affordable Housing and Community Development Law 324 (2006) at 332 (“property taxes have an especially pronounced effect on LIHTC

projects to fail outright⁷. Excessive property taxes, then, directly undermine the LIHTC program's purpose of increasing the supply of affordable housing.⁸ The Appellees here do not assert the extreme view that the public policy that they serve should exempt them entirely from *ad valorem* taxes on their property, although Mr. McNeely and other commentators argue that such exemption is necessary and appropriate. Rather, the Appellees simply insist that the real property in question be accurately valued in accordance with the existing law in West Virginia, and assert that such accurate valuation will not undermine this laudable public policy.

Commentators have recognized that the unusual rules and restrictions imposed on LIHTC properties by federal and state regulation make the valuation of these properties for property tax purposes quite complex.⁹ This complexity undoubtedly explains the wide disparity between how these properties are valued by assessors in various counties in West Virginia. Uncertainty in the face of this complexity may also explain why the Tax Commissioner has failed to exercise his authority to define by legislative rule how these properties are to be valued, and why he sanctions the use of methods by Assessors that are diametrically opposed to each other and to the method used by his own staff.

Despite this complexity, and despite significant differences in property tax law in the

projects, with property taxes often serving as the decisive factor in determining whether to develop a project").

⁷ See Rosenblum, *Assessing the Value of Affordability: Ad Valorem Taxation of Properties Participating in the Low Income Housing Tax Credit Program*, 2 John Marshall Law School Fair and Affordable Housing Commentary 32 (2006) at 37 ("While revenues are limited, operating expenses for affordable housing tend to be similar or higher than those for market-rate units"); McNeely, *supra*, at 333 (Noting that "the Indiana Association for Community Economic Development found that because of restricted rents and marginal cash flows, owners of projects funded through the LIHTC are "unable to charge higher rents and if additional funds are not available, the owners may be forced to discontinue operation. In some cases, this increase in the property tax burden may cause local nonprofit housing corporations to cease to exist."").

⁸ See McNeely, *supra* at 324-5.

⁹ See generally Rosenblum, *supra*.

various states, there has emerged a remarkable convergence in at least some aspects of the question of how LIHTC properties should be valued, both in the courts and in generally accepted appraisal practices. For example, courts are virtually unanimous in holding that the income approach, rather than the cost approach, is more suitable for valuing these properties. When the income approach is used, courts are virtually unanimous in holding that that the actual restricted rents that the owners are constrained to charge should be used, rather than the hypothetical “market-based” rents that unrestricted apartments could bring on the open market.

And while there is less convergence on the issue of whether the value of the tax credits should be included in the appraised value of the property, many of the differences can be explained by disparities in the underlying property tax law, such as whether intangible property is exempt from taxation or whether the state’s definition of “real property” is broad enough to include the tax credits themselves. Given West Virginia’s relatively narrow definitions of the types of property subject to taxation, our exemption of intangible property, and the fact that the tax credits are not owned by the owners of the real property, it is clear that the value of the tax credits should not be included in the appraised value of the property.

The circuit courts in West Virginia are divided on how these properties should be valued. This Court should affirm that the decision below by the Circuit Court of Cabell County correctly interpreted the law in West Virginia, and in doing so should confirm that the law in West Virginia is consistent with the majority view in other jurisdictions and does not undermine the laudable underlying public policy of the LIHTC program established by Congress. There is great value in such consistency, because “without consistent methodology for valuing LIHTC

properties, owners will not have confidence in the financial viability of their properties and they will [bear] a greater risk of default”.¹⁰

II. Standard of Review

A. In the Circuit Court

The Petition for Appeal in this matter correctly asserts that the recent case of *In re Tax Assessment Against American Bituminous Power Partners, L.P.*, 208 W.Va. 250, 539 S.E.2d 757 (2000) sets forth the standard of review under which a circuit court reviews a decision of a county commission sitting as a board of equalization and review; *see also In re Tax Assessment of Foster Foundation's Woodlands Retirement Community*, ___ W. Va. at ___, 672 S.E.2d 150 at 162 (No. 33891, Nov. 5, 2008) (“A taxpayer’s initial avenue for relief from an allegedly erroneous property valuation lies with the county commission, sitting as a board of equalization and review. The burden upon the taxpayer to demonstrate error with respect to the State’s valuation is heavy in these adjudicative proceedings: It is a general rule that valuations for taxation purposes fixed by an assessing officer are presumed to be correct. The burden of showing an assessment to be erroneous is, of course, upon the taxpayer, and proof of such fact must be clear.”) (quoting *American Bituminous*); *accord* Conclusion of Law No. 1, Order Granting Summary Judgment at 9.

B. Before This Court

Syllabus Point 3 in *Foster* provides that “[a]n assessment made by a board of review and equalization and approved by the circuit court will not be reversed when supported by substantial evidence unless plainly wrong.” (citations omitted). There, this Court explained that “[g]enerally, a multifaceted standard of review is applicable to decisions of a circuit court: ‘This

¹⁰ *Id.* at 32.

Court reviews the circuit court's final order and ultimate disposition under an abuse of discretion standard. We review challenges to findings of fact under a clearly erroneous standard; conclusions of law are reviewed de novo.” *Id.*, ___ W. Va. at ___, 672 S.E.2d at 154-155.

III. Statement of Facts

A. Overview of the LIHTC Program

According to the U.S. Department of Housing and Urban Development (HUD), the LIHTC Program is an indirect Federal subsidy used to finance the development of affordable rental housing for low-income households.¹¹ The program, which is based on Section 42 of the Internal Revenue Code¹², was enacted by Congress in 1986¹³ to provide the private market with an incentive to invest in affordable rental housing. Federal housing tax credits are awarded to developers of qualified projects. Developers then sell these credits (at a discount) to investors to raise capital (or equity) for their projects, which reduces the debt that the developer would otherwise have to borrow. Because the debt is lower, a tax credit property can in turn offer lower, more affordable rents. Provided the property maintains compliance with the program requirements, investors receive a dollar-for-dollar credit against their Federal tax liability each year over a period of 10 years.

Each year, the IRS allocates housing tax credits to designated state agencies-typically state housing finance agencies, which in turn award the credits to developers of qualified projects.¹⁴ In West Virginia, the West Virginia Housing Development Fund is responsible for

¹¹¹¹ See <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/> (last viewed February 26, 2009).

¹² 26 U.S.C. § 42.

¹³ Tax Reform Act of 1986, Pub.L. No. 99-514, 100 Stat. 2085 (1986).

¹⁴ <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/allocating.cfm> (last viewed February 26, 2009); Tr. 15-16.

administering the LIHTC Program. Since its inception, this program has produced more than 9,700 affordable rental units.¹⁵ In West Virginia, \$3,980,000 in tax credits is available for allocation in 2009.¹⁶

To be eligible for consideration under the LIHTC Program, a proposed project must:

- Be a residential rental property.
- Commit to one of two possible low-income occupancy threshold requirements.
- Restrict rents, including utility charges, in low-income units.
- Operate under the rent and income restrictions for 30 years or longer, pursuant to written agreements with the agency issuing the tax credits.¹⁷

Project owners may elect one of the following two thresholds:

20-50 Rule: At least 20 percent of the units must be rent restricted and occupied by households with incomes at or below 50 percent of the HUD-determined area median income (adjusted for household size).

40-60 Rule: At least 40 percent of the units must be rent restricted and occupied by households with incomes at or below 60 percent of the HUD-determined area median income (adjusted for household size).

The rent for each unit is established so that tenant monthly housing costs, including a utility allowance, do not exceed the applicable LIHTC rent limit. These limits are based on a percentage of area median income, as adjusted by unit size. The rents can only be increased if the area's median income increases, Tr. 6¹⁸, but in fact, the area's median income has decreased twice since 1990, which reduced the rent that can be charged. Tr. 37.

The LIHTC program requires a minimum affordability period of 30 years (i.e., a 15-year

¹⁵ <http://www.wvhdf.com/developers/lihtcp.cfm> (last viewed February 26, 2009).

¹⁶ http://www.novoco.com/low_income_housing/lihtc/federal_lihtc.php (last viewed February 26, 2009).

¹⁷ <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/eligibility.cfm> (last viewed February 26, 2009). Note that the Appellant's Brief misstates the minimum period as being fifteen years. See *Petitioners' Appellants' Brief* at 6.

¹⁸ References in this format are to the corrected transcript of the February 19, 2008 and February 22, 2008 hearings bearing the Court Reporter's Certification on page 73 dated July 7, 2008.

compliance period and subsequent 15-year extended use period). Some states require a longer affordability period for all LIHTC properties, and other states may negotiate longer affordability periods on a property-specific basis. Tenant incomes are recertified annually to ensure their continued eligibility. The allocating agency is responsible for monitoring compliance with the provisions during the affordability period and must report the results of monitoring to the IRS.¹⁹ If a tenant that has moved in is not eligible to live there, the investor loses his credits for life on that apartment. Tr. 60.

Tax credits can be claimed annually over a 10-year period by the property owner, ten percent annually for ten years.²⁰ However, the developer needs the money immediately to pay for development costs, not ten percent annually for ten years. Accordingly, the developer typically syndicates the credits - *i.e.*, sells the rights to the future credits in exchange for up-front cash. The credit purchaser must be part of the property ownership entity; usually this is accomplished by creating a limited partnership (in which the credit purchaser is a 99%+ limited partner) or a limited liability company (in which the credit purchaser is a 99%+ non-managing member). The general partner is responsible for managing the project and the partnership, while the limited partners are typically limited to a passive investment role.²¹ If the property is sold after the ten year period, the tax credit is gone and can't be transferable to the buyers, but the restrictions continue for the full thirty or more years of the compliance period. Tr. 14-15. The tax credits are subject to recapture for the full period if any of the restrictions are violated; this

¹⁹ *Id.*

²⁰ 26 U.S.C. § 42(b)(2)(B); Tr. 16.

²¹ <http://www.hud.gov/offices/cpd/affordablehousing/training/web/lihtc/basics/syndication.cfm> (last viewed February 26, 2009); Tr. 16, 23, 57-59, 60-61.

possibility gives the original investors an incentive to remain limited partners to protect their interests.

B. The Proceedings Below

The Appellees all appeared before the County Commission of Cabell County sitting as a Board of Equalization and Review (hereinafter the "Board") on February 19 and 22, 2008 and contested the Assessor's valuation of their property. Finding of Fact No. 5, Order Granting Summary Judgment at 3. At that hearing, the Petitioner presented appraisals for each property performed by a licensed professional appraiser who valued the properties substantially below the Assessor's appraised values. Finding of Fact No. 6, Order Granting Summary Judgment at 3. By unanimous vote on February 22, 2008, the Board denied the Petitioner's challenges and upheld the Assessor's appraised values. Finding of Fact No. 9, Order Granting Summary Judgment at 3. By letter dated February 25, 2008, the Board notified the Appellees of its decision and of the final appraised values for tax year 2008 of \$2,952,100 for The Parks, \$3,015,000 for The Hamlets, and \$2,017,000 for Pine Haven. In doing so, the Board set the value of Appellees' property in excess of its true and actual value in contravention of the provisions of W. Va. Code § 11-3-24 and W. Va. Code § 11-3-1 and of Article X, Section 1 of the Constitution of West Virginia.

Pursuant to the provisions of W. Va. Code § 11-3-25, the Appellees then filed individual appeals in the Circuit Court of Cabell County. Finding of Fact No. 11, Order Granting Summary Judgment at 4. Pine Haven's appeal (Civil Action No. 08-C-0223) was assigned to Judge David M. Pancake; The Hamlets' appeal (Civil Action No. 08-C-0224) was assigned to Judge John L. Cummings, and The Parks' appeal (Civil Action No. 08-C-0225) was assigned to Judge Pancake. Finding of Fact No. 12, Order Granting Summary Judgment at 4. Following a hearing conducted

on May 22, 2008, Judge Pancake on May 28, 2008 ordered that the Hamlet's appeal be transferred from Judge Cummings to Judge Pancake, ordered the three cases consolidated as Civil Action No. 08-C-0223 and established a schedule to govern briefing and argument of the consolidated matter. Finding of Fact No. 13, Order Granting Summary Judgment at 4.

On July 11, 2008, the Appellees herein filed a Motion for Summary Judgment and Memorandum of Law in support thereof. Following completion of briefing, by Final Order entered November 12, 2008, Judge Pancake found that there existed no genuine issues of material fact, found that the Appellees were entitled to summary judgment in their favor as a matter of law, and granted each Appellees' motion for summary judgment. The Court further found that the true appraised value of each property was the value determined by the Appellees' appraiser and ordered the Assessor of Cabell County make the appropriate corrections in the tax books for tax year 2008 and ordered the Sheriff of Cabell County to issue the appropriate refund or credit as specified by the provisions of W. Va. Code § 11-3-25. Order Granting Summary Judgment at 13.

C. The Properties in Question

The three properties in question, Pine Haven, The Hamlets, and The Parks, are all LIHTC properties. Tr. 6, 21; Finding of Fact No. 2, Order Granting Summary Judgment at 2. All three are rent restricted, Tr. 12, 13, 21, and all comply with either the 20-50 Rule or the 40-60 Rule. Tr. 6. For example, at the Parks, 13 units are restricted to the 50 percent of area median income limit, and the remainder of the units are restricted to the 60 percent of area median income limit. Tr. 7-8. All three properties are owned by limited partnerships. Tr. 59-60.

Pine Haven consists of one masonry apartment building on an approximately 1.5 acre lot adjacent to Pine Haven Drive in Milton, WV. The three-story mid-rise brick and vinyl 40-unit

apartment building contains a total of 28,143 square feet. There are 30 two-bedroom apartments and 10 three-bedroom apartments. The property is also known as Pine Haven Terrace Apartments and provides housing for seniors citizens. See Appraisal prepared by Mr. Bunch at page 1-2.

The Hamlets consists of seven apartment buildings on approximately 6.05 acres adjacent to Structures Incorporated on Price Industrial Lane in Huntington WV. The buildings are brick and vinyl town homes. There are 38 two-bedroom apartments and 12 three-bedroom apartments for a total of 50 units which contain a total of 51,960 square feet. See Appraisal prepared by Mr. Bunch at page 1-2.

The Parks consists of seven apartment buildings on approximately 8.9 acres adjacent to Work Force WV on Park Street in Huntington WV. The buildings are brick and vinyl town homes. There are 38 two-bedroom apartments and 12 three-bedroom apartments for a total of 50 units which contain a total of 51,960 square feet. See Appraisal prepared by Mr. Bunch at page 1-2; Tr. at 4.

III. Response to Assignments of Error

- A. The Appellants first assign error to the Circuit Court's conclusion that "the income approach is the proper method for valuing Low Income Housing Tax Credit properties." Conclusion of Law No. 13, Order Granting Summary Judgment at 12. The Circuit Court based its conclusion on the testimony of the Appellees' expert witness, multiple cases from other jurisdictions, and two circuit court opinions from West Virginia. In fact, the case law in the United States is virtually unanimous in agreeing that LIHTC properties can most accurately be valued with the income approach. The Circuit Court's conclusion was fully supported by the facts in this case and the applicable law and should be affirmed.
- B. The Appellants' next contend that the Appellees failed to establish the true and actual value of their properties because their values improperly excluded the value of the low income housing tax credits. In fact, it was entirely proper for the Appellees' appraiser to exclude the value of those tax credits, because the tax credits are intangible property and are not subject to taxation by law in West Virginia. Even if the tax credits were taxable, they are not taxable to the Appellees, but to the individual investors who now own them.

The Circuit Court was therefore correct to conclude that the Appellees presented clear and convincing evidence that the appraisal done by Mr. Bunch correctly valued the subject properties.

IV. Argument

A. The Law Regarding the Appraisal of Property Generally

Article X, § 1 of the Constitution of West Virginia directs that “... taxation shall be equal and uniform throughout the State, and all property, both real and personal, shall be taxed *in proportion to its value* to be ascertained as directed by law...” (emphasis added). Two basic tenets of property tax law in West Virginia flow from this section: in order to satisfy the constitutional requirement of equal and uniform taxation, the value of the property must be accurately determined, and that value must be determined “as directed by law”; that is, the same rules must apply to everyone.

The law implementing this provision of our Constitution is found at Chapter 11, Article 3 of the Code of West Virginia, which sets forth the general requirements for assessments of property. W. Va. Code § 11-3-1 provides, in relevant part, that “[a]ll property shall be assessed annually as of the first day of July *at its true and actual value*; that is to say, at the price for which such property would sell if voluntarily offered for sale by the owner thereof, upon such terms as such property, the value of which is sought to be ascertained, is usually sold, and not the price which might be realized if such property were sold at a forced sale,...” (emphasis added). Conclusion of Law No. 3, Order Granting Summary Judgment at 10.

The State Tax Commissioner has promulgated legislative rules, found at Title 110, Series 1P of the Code of State Regulations, which “clarify and implement State law as it relates to the appraisal at market value of commercial and industrial real property.” 110 W. Va. C.S.R. § 1P-1.1. These rules reiterate that the appraised value of commercial and industrial real property

must be its market value, which the rules define as “the price at or for which the property would sell if it was sold to a willing buyer by a willing seller in an arms-length transaction without either the buyer or the seller being under any compulsion to buy or sell”. 110 W. Va. C.S.R. § 1P-2.1.1. Conclusion of Law No. 4, Order Granting Summary Judgment at 11. These legislative rules also require that “[g]enerally accepted appraisal methods [be] used to establish the value of industrial and commercial real properties”. 110 W. Va. C.S.R. § 1P-2.2. All subsequent provisions of the legislative rules, and all of the appraisal methods employed by the assessor of each county in the State, must adhere to these general provisions of the law.²²

Subsection 2.2.1 provides that “[i]n determining an estimate of fair market value, the Tax Commissioner will consider and use *where applicable*, three (3) *generally accepted* approaches to value: (A) cost, (B) income, and (C) market data” (emphasis added). By repeating the “generally accepted” language, this subsection reiterates the requirement that each of the three

²² In the companion cases with which this case has been consolidated, styled *Heathermoor Limited Partnership v. Joseph Alongi, as Assessor of Hancock County, and Virgil T. Helton, West Virginia Tax Commissioner* and *Stone Brooke Limited Partnership v. Phyllis Sisinni, as Assessor of Brooke County, and Virgil T. Helton, West Virginia Tax Commissioner*, No. 34423 and 34424, counsel for the Tax Commissioner takes the altogether remarkable position that “there is no statutory provision which substitutes the Tax Commissioner as the appraiser of commercial real estate like the property whose valuation is at issue before this Court.” Tax Commissioner’s Brief at 1 n. 2.

That litigation position ignores the supervisory role established by the Legislature for the Tax Commissioner. See W. Va. Code § 11-1C-5: “The tax commissioner shall have the power to ... (2) Determine the methods of valuation for both real and personal property...” and W. Va. Code § 11-1C-7(a): “[County Assessors] shall utilize the ... valuation system established by the tax commissioner.” While it is true that the Tax Commissioner’s legislative rules found at Title 110, Series 1P govern the methods of valuation of industrial property appraised by the Tax Commissioner pursuant to W. Va. Code § 11-1C-10, it is no less true that these rules apply to the appraisal of commercial property by the various county assessors. Certainly, the Assessor of Cabell County believes that these rules are applicable, as he has cited these rules repeatedly in his brief to this Court. In fact, the Tax Commissioner concedes this point, because he also cites his own legislative rules in his brief. See Tax Commissioner’s Brief at 11 (arguing that “the cost approach is one of the three recognized methods which are authorized for use by the legislative regulations to appraise property”).

In advancing this litigation position, the Tax Commissioner urges this court to adopt a position that violates the “equal and uniform” provision of the West Virginia Constitution. If next year a different Assessor chooses an entirely different method that undervalues these properties, would the Tax Commissioner still urge this Court to defer to that Assessor’s method?

approaches must be applied in a manner consistent with generally accepted appraisal practices, and also limits the assessor to using only the approaches that are applicable to the particular property being appraised. In *In re Tax Assessment Against American Bituminous Power Partners, L.P.*, *supra*, the West Virginia Supreme Court of Appeals examined Subsection 2.2.1 carefully, and also observed that 110 W. Va. C.S.R. § 1P-2.2.2 “directs that ‘[w]hen possible, *the most accurate form of appraisal should be used*, but because of the difficulty in obtaining necessary data from the taxpayer, or due to the lack of comparable commercial and/or industrial properties, choice between the alternative appraisal methods may be limited’” (emphasis added), and concluded that “[t]he Tax Commissioner is required to ‘consider’ the various approaches to valuation by contemplating the feasibility of utilizing each of the ascribed methods. On the other hand, these methods are to be ‘used’ or actually employed only where ‘applicable’”. *In re Tax Assessment Against American Bituminous Power Partners, L.P.*, 208 W.Va. at 257, 539 S.E.2d at 764. Conclusion of Law #5, Order Granting Summary Judgment at 10.

B. The Methods That Are Applicable in Valuing LIHTC Properties

The Tax Commissioner’s regulations recognize that there are two situations in which one or more of these approaches is simply not applicable; either (1) because of the difficulty in obtaining necessary data from the taxpayer, or (2) due to the lack of comparable commercial and/or industrial properties. 110 W. Va. C.S.R. § 1P-2.2.2. In fact, in this case, both parties agreed that the latter circumstance was present and therefore agreed that the market data approach could not be used. Conclusion of Law No. 8, Order Granting Summary Judgment at 11.

While in this case, the Assessor asserts that the results of his cost approach most accurately reflect the fair market value of the property in question, and the taxpayers rely on the

value established by their appraiser's income approach, it should be emphasized that *this case is not simply a dispute over whether the cost approach or the income approach is better suited to valuing LIHTC properties*. This is so because the objective of both approaches is the same: to yield an accurate estimate of the true and actual value of the property. Thus, if both approaches are properly performed, both should yield similar values.

The Tax Commissioner implicitly recognizes this fact in his brief in the *Heathermoor* and *Stone Brooke* cases when he argues that, for the Stone Brooke property in Brooke County, the close proximity (within seven percent) between the Tax Department's income valuation and the Assessor's cost valuation "would tend to support each other". Tax Commissioner's Brief at 12. Similarly, in this case, the Assessor, reportedly at the behest of the Tax Commissioner, used the income approach to "confirm" the results of his cost approach. Conclusion of Law No. 11, in part, Order Granting Summary Judgment at 11. Yet here, the Assessor's cost approach values were more than *three times* those presented by the Appellees' appraiser, which were determined with the income approach (\$2,952,100 vs. \$750,000 for The Parks, \$3,015,000 vs. \$900,000 for The Hamlets, and \$2,017,000 vs. \$500,000 for Pine Haven). If close proximity of results confirms both, then the wide disparity in this case between the results of the Assessor's cost approach and the taxpayers' income approach clearly indicates that something is wrong.

In fact, as will be demonstrated below, the taxpayers' income approach correctly determined the true and actual value of the LITHC properties, while the Assessor's value by the cost approach is excessive, both because it includes value that is not taxable to the owners of the real property and because it improperly failed to exclude items of depreciation.

C. The Income Approach

1. The Income Approach is the Generally Accepted Appraisal Method for Valuing LIHTC Properties

The Appellees presented an appraisal for each property performed by Mr. David E. Bunch. Findings of Fact Nos. 6, 17, Order Granting Summary Judgment at 3, 5. Mr. Bunch is Licensed Certified General Real Estate Appraiser and a Licensed Certified Residential Real Estate Appraiser in West Virginia and has 46 years of real estate experience. See page titled "Qualifications of David E Bunch, Appraiser" included with each appraisal; Finding of Fact No. 7, Order Granting Summary Judgment at 3. Each appraisal; states at page 2:

Due to the subject property specific restrictions, the Cost Approach and the Sales Comparison Approach were not considered. The restrictions for the construction would make it cost prohibitive for a purchaser in the open market based upon the funding restrictions. The sale would be influenced solely by the income produced per unit which would produce a value by the income approach. Therefore, the Income Approach was considered applicable, and the analysis was performed.

Finding of Fact No. 17, Order Granting Summary Judgment at 5.

The Tax Commissioner's definition of commercial property found at 110 W. Va. C.S.R. § 1P-2.3.3 emphasizes its nature as "income producing property" and specifically mentions apartment buildings:

"Commercial property" means income producing real property used primarily but not exclusively for the sale of goods or services, including but not limited to offices, warehouses, retail stores, apartment buildings, restaurants and motels.

Mr. Bunch also testified that, to his knowledge, the income approach is the only way to properly appraise LIHTC properties, Tr. 4, because "[t]hat's the way any person that would be in the business would buy these, is the income that it produces after the net of operation and what is that worth... Value has got to come from 40 unit apartments from the income. That's why you buy it." Tr. 11-12, *see also* Tr. 14, 27. Mr. Childers' testimony was consistent with that offered

by Mr. Bunch. Tr. 37 (“Ask an investor, what would he pay for it. Well, he's going to pay off the income”).

While this Court has not addressed the issue of how to properly value LIHTC properties, virtually unanimous weight of authority from other states indicates that the income approach is the most appropriate approach to use for valuing these properties. *Rosenblum, supra*, at 34; *Deerfield 95 Investor Associates, LLC v. Town of East Lyme*, 1999 WL 391099, 25 Conn. L. Rptr. 51 (1999) (“As a general rule, the income approach provides the most critical method of valuing LIHTC properties); *Huron Ridge, L.P. v. Township of Ypsilanti*, 275 Mich.App. 23, 737 N.W.2d 187 (2007) (“The parties agreed that the appropriate appraisal method for the property was the income method.”); *Town Square Ltd. Partnership v. Clay County Bd. of Equalization*, 2005 SD 99, 704 N.W.2d 896 (2005) (“In this case, both sides agreed that the income capitalization approach was the most reliable method for determining the true value of the Town Square apartment building.”).

At least three circuit court decisions in West Virginia have also upheld the use of the income approach for LIHTC or other special purpose residential multi-unit properties. In *Providence Green LLC v. Assessor, et al.*, Civil Action Nos. 07-CAP-7 and 08-CAP-14, the Circuit Court of Ohio County, Judge Wilson presiding, found that, in light of the taxpayer’s evidence that “the Income approach was the most appropriate method to value this LIHTC property”, the taxpayer met its burden to prove the property’s true and actual value by introducing an appraisal based on that approach.

In the case of *In re 1994 Tax Assessment of Twin Oaks Plaza et al.*, Civil Action No. 94-C-78-H, the Circuit Court of Fayette County, West Virginia, the Honorable John W. Hatcher, Jr.,

presiding, found as a matter of law that the income approach was the “appropriate, realistic, accurate, fair and correct method by which to ascertain” the value of the fee simple estate of the subject property, which in that case was a H.U.D. Section 202 and Section 8 housing project, not an LIHTC property.

Finally, the Court below found that “Given the testimony of Mr. Bunch, the multiple cases from other jurisdictions, as well as two circuit court opinions from West Virginia [*Providence Green, supra* and *Twin Oaks Plaza, supra*], the Petitioners have clearly demonstrated that the income approach is the proper method for valuing Low Income Housing Tax Credit properties”. Conclusion of Law #10, Order Granting Summary Judgment at 10.

Neither the Tax Commissioner nor the Assessor claims that the income approach is not applicable to valuing LIHTC properties. In the companion cases, in fact, the Tax Commissioner’s appraiser used the income approach to value the properties, which he now asserts “adds some value.” Tax Commissioner’s Brief at 12. In this case, the Court below concluded that “[t]he fact that the Respondents performed their own income approach appraisal as a check on their cost approach demonstrates that they understand that the income approach is likely the best way to value the property.” Conclusion of Law #11, Order Granting Summary Judgment at 11.

2. The Use of Restricted Rents, rather than Market Rents, in the Income Approach is the Generally Accepted Appraisal Practice

The income approach computations in the appraisals submitted by the Appellees in these cases were based solely on the actual, restricted rents that the owners actually receive. The Appellees’ appraisals state:

The appraiser used the specific rental income to the property since the amounts were dictated by the restrictions, and would not, nor could reflect an open market rent.

Appraisals at 2.

The Appellants in this case, however, assert that the use of the restricted rents contravenes 110 W. Va. C.S.R. § 1P-2.2.1.2, which provides that “[t]he present fair market value of the property shall then be determined by dividing the annual *economic rent* by the capitalization rate” in the income approach, and 110 W. Va. C.S.R. § 1P-2.3.6 which defines “[e]conomic rent” as “the rental amount which a space or property would attain in the open market at the time of appraisal, whether it is lower, higher or the same as the actual contract rent”. As the Appellees demonstrated in their Response to the Petition for Appeal in this matter, this assertion cannot be correct for at least two reasons. First, the virtually unanimous weight of authority in the United States supports the use of the restricted rents, rather than market rents, in the income approach. Secondly, the term “economic rent” in the Tax Commissioner’s legislative rules must be interpreted to require the use of the restricted rents required by law, rather than the market based rents. *See* Response to the Petition for Appeal at 16-25.

The Assessor’s assertion that the term “economic rent” here means the market-based rent that the units could receive on the open market were they not subject to rent restrictions for 30 or 40 years is at odds with the position taken by the Tax Commissioner in the companion cases, where he concedes that restricted rents should be used in the income approach. *See* Tax Commissioner’s Brief at 18 (“[t]his Court should adopt the analysis of the Courts who have found that the tax credits must be included in the value *along with the rent restrictions*”). Because the Tax Commissioner has the responsibility to determine “the methods of valuation for

both real and personal property”, his litigation position here renders the Appellant’s argument as to the use of market-based rents moot.

D. The Assessor’s Cost Approach

Testifying for the Assessor, Mr. Wheeler stated that the Assessor is constrained to using only the mass appraisal system provided by the State Tax Commissioner. Tr. 43. The State’s mass appraisal system values improvements by the cost approach; that is, by equating value with the replacement cost less depreciation. Tr. 33, 40²³, 55, 56.

However, Mr. Bunch and Mr. Peoples, speaking on behalf of the Appellees, testified that for these properties, the cost approach is inapplicable. Tr. 14, 33. The appraisals also indicate Mr. Bunch’s opinion that the restrictions on the properties’ use make the cost approach inappropriate. Appraisals at 2. The weight of authority from other jurisdictions supports the Appellees’ position that the cost approach is not appropriate for valuing LIHTC properties, at least if it fails to include allowances for functional and economic obsolescence. Here, the Assessor failed to recognize the presence of both functional and economic obsolescence, and he improperly included value for the tax credits without offering evidence as to the value he placed on those credits or as to how that value was determined.

1. Some Courts Have Held That the Cost Approach Is Not Appropriate for Valuing LIHTC Properties

The pole star of property taxation West Virginia is that all property must be appraised at its fair market value, in other words, the price that a willing seller will accept from a willing buyer. The testimony in this case reflects that an investor will only invest if the potential income from the property is sufficient to justify the risk. In *Cascade Court Limited Partnership v.*

²³ Mr. Peoples uses the term “value approach” in place of the term “cost approach”.

Noble, 105 Wash.App. 563, 20 P.3d 997 (2001) the Court of Appeals of Washington, Division 1 summarized some of the issues with the use of the cost approach for these properties:

[W]e do note that the Department of Revenue, as *amicus*, has argued that "the preferred approach to valuing low-income housing ... is to capitalize net operating or actual income." DOR Br. at 10 (footnote omitted). Furthermore, the cost method is generally preferred only where the properties being appraised "are not amenable to valuation by the income capitalization approach." APPRAISAL INSTITUTE, *THE APPRAISAL OF REAL ESTATE* 338 (11th ed.1996). Finally, the appraisal literature and case law regarding rent-restricted low-income housing argue against the use of the cost method. See, e.g., David C. Nahas, *Appraising Affordable Multifamily Housing*, Appraisal Journal, July 1994, Vol. 62 No. 3; Richard E. Polton, *Valuing Property Developed with Low Income Housing Tax Credits*, The Appraisal Journal, July 1994; Laurence G. Allen, *Valuing Subsidized Housing for Property Tax Purposes*, Appraisal Journal, January 1986, Vol. 54, No. 1. See also *Community Development Co. of Gardner v. Board of Assessors of Gardner*, 377 Mass. 351, 385 N.E.2d 1376 (1979) (construction costs of federally rent-controlled low-income housing overstate the market value of a project since, in the absence of governmental subsidies, the rental stream produced by the property would not justify actual expenditure on construction); *Bayridge Assoc. Ltd. Partnership v. Dep't of Revenue*, 13 Or. Tax 24, 31 (1994 (due to governmental restrictions cost approach would give excessive indication of value), *aff'd*, 321 Or. 21, 892 P.2d 1002 (1995)).

Cascade Court Limited Partnership v. Noble, 105 Wash.App. 563 at 570 n. 33, 20 P.3d at 1002 n. 33.

Restricted rents aren't the only aspect of an LIHTC project that makes the use of the cost approach problematic. In *In Re 1994 Tax Assessment of Twin Oaks Plaza et al.*, *supra*, the Court held that the use of the cost approach did not arrive at the true and actual value of the property, at least partly because "[t]he Twin Oaks Plaza, constructed to qualify for participation in the H.U.D. Section 202 and Section 8 program, was built with various safety features and other amenities which, but for participation in the H.U.D. program, would, in all probability, not have been included in the design and construction of the building", *In Re 1994 Tax Assessment of Twin Oaks Plaza et al.*, *supra*, Finding of Fact No. 7, and "[w]hile adding substantial cost to the construction of the building, these safety features and other amenities do not now materially

affect the fair market value of the fee simple estate of the Petitioner.” *Id.*, Finding of Fact No. 8. LIHTC projects are subject to similar requirements that add substantial cost to their construction; those requirements are implemented in the required restrictive covenants that run with the land and that require adherence to the Fair Housing Act. *See, e.g., Montana Fair Housing, Inc. v. American Capital Development, Inc.*, 81 F.Supp.2d 1057 (D.Mont., Nov 30, 1999); *see also* Penna, *supra*, at 56-57.

In both the *Heathermoor* and *Stone Brooke* cases now before this Court, the Circuit Court ruled that the taxpayers there failed to prove by clear and convincing evidence that the Assessor’s use of the cost approach for recently constructed rent restricted LIHTC properties was inappropriate. The Court recognized that there was then a split among the lower courts that had addressed the issue of how to properly value LIHTC properties, citing two cases: *In re: 1994 Prop Tax Assessment of Twin Oaks Plaza, supra*, in which the Court ruled that the income approach should be used, and *Shepherds Glen Ltd. P’shp. v. Bordier*, Civil Action No. 03-C-71 (Jefferson Cty., W. Va. Sept. 22, 2003, which upheld the Assessor’s use of the cost approach.

In *Shepherds Glen*, the Court ruled that a taxpayer’s appraisal based on the income approach and using restricted or “basic” rents rather than market or “economic” rents did not comply with the Tax Commissioner’s rules and thus must be disregarded. Findings and Conclusions No. 20. The four properties in question were not, however, LIHTC properties, but were “Section 515” properties financed and administered under Section 515 of the Rural Housing Program. Findings and Conclusions No. 17. Under this program, the owners are provided low interest mortgage loans, *id.*, whereas an LIHTC (and the properties at issue in this case) are subject to conventional mortgages obtained on the open market. Tr. 61.

The Court in *Shepherds Glen* stated that it “believes that the approach taken by the Ohio

Courts, that market value should be determined uncomplicated by encumbrances, and free of deed restrictions and restrictive contracts with the federal government is the best approach”.

Findings and Conclusions No. 23. To support this belief, it cited several Ohio cases, including *Alliance Towers, Ltd. v. Stark County Bd. of Revision*, 37 Ohio St.3d 16, 523 N.E.2d 826 (1988).

There is no indication, however, that the Court in *Shepherds Glen* took into account the fact that the properties in question in *Alliance Towers* were federally subsidized housing, not Section 515 housing, and thus, unlike the properties in *Shepherds Glen*, the rents in *Alliance Towers* were higher than market based rents²⁴. Thus, using the Court’s logic in *Shepherds Glen*, the use of market based rents in the income approach for an LIHTC property, where market based rents are higher than the actual restricted rents²⁵, would result in the inclusion of the value of the governmental program in the value of the property, which is exactly the opposite result that the Ohio cases upon which the Court based its decision avoided. See *Inclusion of Intangible Asset Values in Tangible Property Tax Assessments*, 90 ALR 5TH 547, § 9[b].

Moreover, in *Woda Ivy Glen Ltd. Partnership v. Fayette Cty. Bd. of Revision*, 121 Ohio St.3d 175, 902 N.E.2d 984 (2009), the Ohio Supreme Court recently reached exactly the opposite

²⁴ Similarly, the properties in question in the other cases cited by the Court in *Shepherds Glen* were also subsidized by the federal government. See *Canton Towers, Ltd. v. Board of Revision of Stark County*, 3 Ohio St.3d 4, 444 N.E.2d 1027 (1983); *Sunset Square Ltd. v. Miami County Bd. of Revision*, 50 Ohio St.3d 42, 552 N.E.2d 632 (1990); *Loveland Pines v. Hamilton Cty. Bd. of Revision*, 66 Ohio St.3d 387, 613 N.E.2d 191 (1993); *Villa Park Ltd. v. Clark Cty. Bd. of Revision*, 68 Ohio St.3d 215, 625 N.E.2d 613, (1994); *Delhi Estates, Ltd. v. Hamilton Cty. Bd. of Revision*, 68 Ohio St.3d 192, 625 N.E.2d 594, (1994). See also *Oberlin Manor, Ltd. v. Lorain County Bd. of Revision*, 45 Ohio St.3d 56, 543 N.E.2d 768 (1989) (citing *Alliance Towers*).

²⁵ Market rents for the Cabell County properties are higher than the restricted rents. Mr. Dotson testified that the properties in question normally would collect an \$800 to \$900 a month rental fee based on the market in Cabell County; Tr. 11, and the Assessor placed the market value of the apartments at The Parks and The Hamlets at an average of \$700 each. Tr. 56. However, the actual restricted rents are less than \$600 for a two bedroom apartment. Tr. 11. Therefore, to exclude the value of the tax credits, restricted rents must be used in the income approach.

conclusion on the import of the *Alliance Towers* decision in an LIHTC situation:

Although broadly stating the generalization that “[i]t is the fair market value of the property in its unrestricted form of title which is to be valued,” *Alliance Towers, Ltd.*, 37 Ohio St.3d at 23, 523 N.E.2d 826, the court's objections to BTA's valuations consisted of three much more concrete points... All of these considerations led the court to conclude that the BTA should value Section 8 properties in accordance with methods that *disregarded* the affirmative value of the subsidies conferred by the federal government....Thus, in spite of the sweeping language of *Alliance Towers*, the plain import of the decision lies in preventing the affirmative benefit of government subsidies from inflating the value of the property for tax purposes”.

Woda Ivy Glen, 121 Ohio St.3d at 182, 902 N.E.2d at 991. The Court held that “The [Board of Tax Appeals] erred by holding that the effect of [the use restrictions imposed under I.R.C. 42] must be disregarded and by reverting to a cost-based valuation that improperly reflects the affirmative benefit of the tax credits, which constitute a separable intangible asset.” *Id.*, 121 Ohio St.3d at 184, 902 N.E.2d at 992. To the extent that the Court in *Shepherds Glen* relied on the Ohio cases for the general proposition that market based rents, rather than actual rents, should be used in the income approach, it clearly misconstrued the law in Ohio. There was, simply stated, no basis for the Court’s decision in *Shepherds Glen* to reject the taxpayer’s income approach in favor of the cost approach.

Thus, the results in *Heathermoor and Stone Brooke* are contrary to the result in *In re 1994 Property Tax Assessment of Twin Oaks Plaza*, contrary to the law in Ohio as reflected by *Woda Ivy Glen, supra*, contrary the position taken by the Tax Commissioner’s appraiser in *Heathermoor and Stone Brooke*, and are contrary to the great weight of authority from other jurisdictions that the income approach, not the cost approach, is the better way to value these properties. The Tax Commissioner cites neither legal authority nor any authority on generally accepted appraisal practices to refute this conclusion.

2. If the Cost Approach is Used, Obsolescence Must Be Considered

While the income approach is the preferred approach to valuing LIHTC properties, the cost approach can also be used if properly applied. Where the cost approach is used, courts generally recognize that both functional and economic obsolescence must be considered. The Tax Commissioner's rules for valuing commercial and industrial real estate, in fact, require that both be considered in the cost approach:

Cost Approach - To determine fair market value under this approach, replacement cost of the improvements is reduced by the amount of accrued depreciation and added to an estimated land value. In applying the cost approach, the Tax Commissioner will consider three (3) types of depreciation: physical deterioration, functional obsolescence, and economic obsolescence.

110 W. Va. C.S.R. § 1P-2.2.1.1 (in part).

In *Cascade Court Limited Partnership v. Noble, supra*, the Court held that both forms of obsolescence should be considered in the cost approach:

An assessor using the cost method should make allowances for functional [FN31] and economic [FN32] obsolescence depreciation.

FN31. "Incurable functional obsolescence is 'Functional obsolescence that results from structural deficiencies or superadequacies that the prudent purchaser or owner would not be justified in replacing, adding, or removing, because the cost of effecting a cure would be greater than the anticipated increase in utility resulting from the replacement, addition or removal.' (Footnotes omitted.) Tax credit properties are often superadequate due to unique property characteristics and development expenses.

FN32. The deed restrictions affect the income-producing ability of the projects and thus affect their value. As a result, if the Assessor considers the deed restrictions' effect on the rental income generated by the projects, the Assessor may conclude that the deed restrictions cause the projects to suffer economic obsolescence.

Cascade Court Limited Partnership v. Noble, 105 Wash.App. at 570, 20 P.3d at 1002 (citations omitted). See also *Walworth Affordable Housing, LLC v. Village of Walworth*, 229 Wis.2d 797,

803, 601 N.W.2d 325, 328 (Wis.App., 1999) (“Because the Board conducted a cost approach assessment relying solely on the insurance replacement value of WAH’s property, which did not include consideration of the property’s economic obsolescence, we agree and affirm the circuit court’s order”).

The definitions of functional and economic obsolescence in *Cascade Court* are consistent with the Tax Commissioner’s definitions. 110 W. Va. C.S.R. § 1P-2.3.8 defines “functional obsolescence” as “[t]he loss of value due to factors such as excess capacity, changes in technology, flow of material, seasonal use, part-time use or other like factors. The inability to perform adequately the function for which an item was designed”; and 110 W. Va. C.S.R. § 1P-2.3.5 defines “economic obsolescence” as “a loss in value of property arising from ‘Outside Forces’ such as changes in use, legislation that restricts or impairs property rights, or changes in supply and demand relationships”. There is no evidence in the record of this case that the Assessor considered either functional or economic obsolescence in his appraisal of these properties, despite the fact that functional obsolescence (in the form of the superadequacies required by federal law²⁶) and economic obsolescence (in the form of the restrictions on the properties use and on the rents that can be charged) are apparent.

To be clear, the Appellees do not assert that the simple fact that the Assessor here used the cost approach was, in and of itself, improper. Rather, it was the Assessor’s failure to *properly execute* the cost approach by failing to account for functional and economic obsolescence that contributed to the overvaluation of the properties in question. In this case, the

²⁶ The cost of construction of such government subsidized housing for the elderly and those with low incomes tends to be higher than the cost of a conventional apartment complex due to the extra features required by the minimum property standards and the payment of Davis-Bacon wage rates to the construction workers. *See, e.g., Alliance Towers, Ltd. v. Stark County Bd. of Revision*, 37 Ohio St.3d 16 at 21 n. 4, 523 N.E.2d 826 at 830 n. 4 (1988). Therefore, the apartment buildings under consideration in that Ohio case were constructed at a cost greater than could be justified by market rents. *Id.*, 37 Ohio St.3d 16 at 22, 523 N.E.2d 826 at 831.

Appellants vigorously defend the Assessor's discretion to choose which approach to use to value these properties, but nowhere do they assert that the Assessor properly performed the approach that he chose or was required to use. The Assessor simply used the computer system provided by the Tax Commissioner and valued these apartment buildings as if they were typical commercial properties, free to charge whatever rents the market would bear, and completely ignored their participation in the LIHTC program.

E. The Differences Between the Assessor's Cost Approach and the Appellees' Income Approach

The objective of all three approaches to value (cost, income, and market data) is the same: the determination of the fair market value of the subject property. W. Va. Const. art. X § 1; W. Va. Code § 11-3-1; 110 W. Va. C.S.R. § 1P-1.1. In this case, the magnitude of the differences between the Assessor's values by the cost approach and the taxpayers' appraiser's values by the income approach is large enough to raise immediate concerns. Certainly, the Assessor here questioned the magnitude difference between the (relatively larger) cost to construct the subject properties and the (relatively lower) values derived by the Appellees' appraiser. See Tr. 22:

MR. PERRY: I'd like to know, for our clarification, too, why so much money would be spent on a property that would generate such a small income.

MR. ADKINS: That's what I'm missing here.

MR. PERRY: I mean somebody is making money; correct? Somebody has got to be making good money on these properties.

See also Tr. 28-29. Mr. Perry also questioned why the property would be insured for \$4 million if it was worth less than \$1 million. Tr. 27-28.

These are certainly valid questions, and they have equally valid answers. First, there is a difference between the amount for which the property is insured, which is the full cost to replace

the buildings and contents in the event of a fire or other catastrophic loss, and the “true and actual” value for property tax purposes, which is defined in the cost approach as the replacement cost of the improvements *less the amount of all forms of accrued depreciation* (physical deterioration, functional obsolescence, and economic obsolescence). 110 W. Va. C.S.R. § 1P-2.2.1.1. In other words, the amount for which the property is insured will *always* be significantly higher than the true and actual value of the property for property tax purposes. *See, e.g., Walworth Affordable Housing, supra*, 229 Wis.2d at 803, 601 N.W.2d at 328 (“Considering the insurance replacement value alone does not demonstrate the property’s fair market value because it neglects the economic obsolescence”).²⁷

Secondly, the Appellants argue that the difference between the cost to construct the buildings and the correct appraised value is the value of the tax credits, and assert that the tax credit should be included in the value of the property, and in effect argue that the Appellees’ income approach should have included some value for the tax credits. There are several problems with their argument.

First, as will be explained below, while some of the difference between the results of the cost approach and the income approach are attributable to the value of the tax credits, some of the difference is also attributable to economic obsolescence. Secondly, as also discussed below, even if the entire difference were attributable to the value of the tax credits, that value is exempt

²⁷ Lest this Court be misled, the Tax Commissioner’s brief accurately states that “[f]urthermore, the Brooke County Assessor’s appraisal is lower than the amount of fire insurance which the Taxpayer has on the apartment complex (Stone Brooke Tr. at 20) and is lower than the appraisal done by the Tax Commissioner.” Tax Commissioner’s Brief at 6. It also accurately notes that “[t]he Taxpayer’s representative acknowledged that the fire insurance on the property is based upon replacement cost, which is in excess of the Assessor’s appraisal. (Tr. at 19 and 20). As Appraiser Goff testified, the amount of fire insurance ‘would be another measure of value, what a third party would consider just compensation.’ (Tr. at 20).” *Id.* at n. 6. The Tax Commissioner, however, *never* himself asserted that the amount for which the properties were insured against loss due to fire or other casualty is a direct indication of the true and actual value of the property for *ad valorem* tax purposes, an assertion that he knows full well to be incorrect.

from taxation and/or is not taxable in West Virginia, at least to the Appellees. Finally, even if the value of the tax credits was taxable to the Appellees, the Assessor in this case failed both to determine the amount of economic and functional obsolescence present and failed to determine the value of the tax credits by any generally accepted appraisal technique. Thus, the Court below correctly held that the Assessor failed to meet his burden of production.

1. The Difference is At Least Partly Attributable to Economic Obsolescence

In *Hometowne Associates, L.P. v. Maley*, 839 N.E.2d 269 at 280 (2005), the taxpayer argued that the difference between the results of the cost approach and the income approach was a direct measure of the economic obsolescence present in the property, which is the general rule in Indiana. See *Lacy Diversified Indus., Ltd. v. Dep't of Local Gov't Fin.*, 799 N.E.2d 1215, 1224-25 (Ind. Tax Ct.2003); *Canal Square Ltd. P'ship v. State Bd. of Tax Comm'rs*, 694 N.E.2d 801, 806-807 (Ind. Tax Ct.1998); *Thorntown Tel. Co. v. State Bd. of Tax Comm'rs*, 588 N.E.2d 613, 619 (Ind. Tax Ct.1992); see also *Pedcor Investments v. State Bd.*, 715 N.E.2d 432, 437 (Ind. Tax 1999) (concluding that LIHTC deed restrictions may constitute economic obsolescence). In the case at bar, if the entire difference is taken as the amount of economic obsolescence present in this facility as suggested by *Hometowne Associates*, then the difference entirely disappears; the original result of the Assessor's cost approach less these amounts for obsolescence exactly matches the result of the income approach:

Property	Assessor's Appraised Values (Cost Approach)	Taxpayer's Income Approach (Income Approach)	Indicated Economic Obsolescence
The Parks	\$2,952,100	\$750,000	\$2,202,100
The Hamlets	\$3,015,000	\$900,000	\$2,115,000
Pine Haven	\$2,017,000	\$500,000	\$1,517,000

In this case, the Assessor's application of the cost approach without consideration of obsolescence fails to take into consideration the fact that the subject property is an LIHTC

property and that fails to consider government-mandated restrictions on rent and rentals, additional costs and expenses, illiquidity, and difficulty in attributing the value of the principal benefits of LIHCT projects to the related properties. *See Rosenblum, supra*, pp. 36-38. Here, obsolescence is present both as functional obsolescence (because the facility is ‘superadequate’ for the purpose for which it is actually used) and as economic obsolescence (because of the external rent restrictions). Attributing the difference between the results of the cost approach and the income approach to obsolescence, then, is required to properly value this property. The Assessor valued the properties by the cost approach without deduction for functional or economic obsolescence, and thus failed to recognize the reduction in value mandated by the governmental regulations and restrictions on rent under which the Appellees must operate for 30 or 40 years. Because the Assessor failed to introduce any evidence of a deduction for functional or economic obsolescence or of the value he assigned to the tax credits, the Circuit Court properly concluded that “one cannot say that the Assessor’s valuation is supported by substantial evidence”. Conclusion of Law No. 16 (in part), Order Granting Summary Judgment at 12.

2. If the Tax Credits are Taxable, the Difference is Attributable Both to Economic Obsolescence and the Value of the Tax Credits

The taxpayer in *Hometowne Associates* also presented an alternative calculation, in which the difference between the results of the cost approach and the income approach was a direct measure of *both* the economic obsolescence present in the property and the value of the tax credits. If the value of the tax credits was not considered, the taxpayer claimed an 84.4% reduction from the value as determined by the cost approach; if they were considered, the reduction claimed was 31.3%.²⁸ The Court held that the taxpayer had “established a *prima facie*

²⁸ It should also be noted that in *Hometowne Associates*, the property participated in two federal programs. The owners had been allocated tax credits which they sold to investors under the LIHTC program, and the property was also subject to the provisions of Section 8 of the United States Housing

case that it was entitled to an obsolescence depreciation adjustment of *at least* 31.3%.” *Id.* at 277 (emphasis added). Since the Assessor failed to meet its burden to rebut the taxpayer’s *prima facie* case, the Court remanded the case to the Indiana Board of Tax Review with instructions to order the Assessor to apply a 31.3% reduction. *Id.* at 280-281. The Court selected the lower amount because, as the Tax Commissioner recognizes, Indiana is a jurisdiction in which the value of the tax credits must be included to arrive at the value of the low income housing. See Tax Commissioner’s Brief at 16, citing *Rainbow Apartments, supra*. In fact, however, while decisions from other states are split on this issue, in West Virginia, any value for the tax credits cannot be considered in the value of the real estate, because the tax credits are intangible property and are exempt from taxation. Moreover, they are exempt because they meet neither the definitions of real property or personal property. Finally, in West Virginia, the owners of property are responsible for the property taxes thereon, and the taxpayers here don’t own the tax credits and it is improper to include their value in the assessments.

3. LIHTC Tax Credits are Exempt from Taxation as Intangibles

The tax credits are not taxable in West Virginia because they are a form of intangible property that by law is exempt from taxation. Article X section 1a of the West Virginia Constitution provides, in part:

no intangible personal property shall be subject to such taxation save for and except as provided by the legislature by general law enacted after the ratification of the amendment of this section in the year one thousand nine hundred eighty-four.

Act of 1937, which is administered by the Department of Housing and Urban Development (HUD). *Id.* at 271. Unlike the situation before this Court, the latter program set contract rents above market rents. *Id.* at 280. The amount of economic obsolescence due to restricted rents was undoubtedly offset in some measure by the increased rents realized as a result from the project’s participation in the Section 8 program.

The exemption of intangible personal property from property taxation was implemented by the West Virginia Legislature and was implemented fully for tax year 2003 and thereafter. W. Va. Code § 11-1C-1b.

Many courts have concluded that the tax credits are intangible property and are thus exempt from taxation under the jurisdiction's constitution or statutes. Most recently, the Ohio Supreme Court in *Woda Ivy Glen, supra*, reaffirmed that "'tax shelter advantages' constituted 'intangible items' that '[did] not make the real estate more valuable.'" *Id.*, 121 Ohio St.3d at 182, 902 N.E.2d at 991, citing *Alliance Towers, supra*. It explained that

As for the tax credits themselves, we discern ample reason to disregard them as constituting a part of the value of the realty to the extent that tax benefits are transferred apart from any transfer of the underlying fee interest in the property. As discussed, the method of pursuing an LIHTC development involves "syndicating" the credit by selling passive investment (in this case limited-partner) interests to entities that can benefit from the tax credit. This means that (1) the proportionate interest in the tax credits themselves is transferred apart from any transfer of the entire legal fee interest in the property, and (2) the value that the purchaser places on the credit is driven primarily by the purchaser's particular tax considerations rather than any future value anticipated from the real property itself. As a result, the tax credits qualify as intangible interests separable from the real property.

Woda Ivy Glen, supra, 121 Ohio St.3d at 183 n. 4, 902 N.E.2d at 992 n. 4. There, as here, the assessing authority [the auditor] used the cost approach, and the Court held that the result of the cost approach "improperly reflects the affirmative benefit of the tax credits, which constitute a separable intangible asset." *Id.* 121 Ohio St.3d at 184, 902 N.E.2d at 993; *accord Twin Oaks Plaza, supra*.

The Court in *Cascade Court Limited Partnership v. Noble, supra*, also held that "the [Board of Tax Appeals] erred in holding that the federal tax credits received by the appellants should be included in the assessed value of the projects. Tax credits are intangible personal property and thus are not subject to real property taxation. The Assessor should not take the tax

credits into account in the assessment of the property” (citations to statute omitted). *Id.* 105 Wash.App. 570-571, 20 P.3d 1001-1002.

In *Maryville Properties, L.P. v. Nelson*, 83 S.W.3d 608 (2002), the Missouri Court of Appeals, Western District described the LIHTC program as follows:

The LIHTC program is intended to motivate private investment by providing income tax credits which directly offset the federal income tax obligation of the individual investor. The individual investors in the Maryville property received such income tax credits through the Missouri Housing Development Commission (MHDC), a state agency established pursuant to RSMo. § 215.020. This program also supplied state income tax credits to the investors.

According to the testimony, the individual investor is motivated solely by the tax benefits. The tax credits expire after ten years. The tax credits are "sold" to the individual investor on a discounted basis.

Maryville Properties, L.P. v. Nelson, 83 S.W.3d at 611. The Court then held:

LIHTCs make no direct contribution to the market value of these housing projects. They are intangible property. There is no statutory authority for the consideration of these tax credits in real estate tax appraisal in Missouri.

Maryville Properties, L.P. v. Nelson, 83 S.W.3d at 617.

In *Cottonwood Affordable Housing v. Yavapai County*, *supra*, the Tax Court of Arizona relied heavily on the *Maryville Properties, L.P. v. Nelson* case and on the fact that the Arizona Administrative Code requires Arizona appraisers comply with the Uniform Standards of Professional Appraisal Practice (“USPAP”) when performing appraisals. Since Advisory Opinion 14 of the Appraisal Standards Board recognized that “LIHTCs are an example of an incentive that results in intangible property rights..., the Court found that:

the credits constitute intangible property and should not be added to the value of Cottonwood's property or considered as part of Cottonwood's income stream. LIHTCs are intangible because they are sums of money being paid by the federal government as an incentive to invest in the project and are not income flowing from the rental of the property.

Cottonwood Affordable Housing v. Yavapai County, 205 Ariz. at 429, 72 P.3d at 359. It also observed that “*Cascade Court Ltd.* also found that, ‘tax credits are intangible personal property and thus are not subject to real property taxation.’” *Cottonwood Affordable Housing v. Yavapai County*, 205 Ariz. at 430, 72 P.3d at 360 (citation omitted). The pronouncement of the Appraisal Standards Board is certainly indicative of generally accepted appraisal practice, and thus of the proper treatment of the tax credits. Since the tax credits are intangible, rather than tangible, property, they are not subject to taxation in West Virginia.

4. Tax Credits Are Neither Real nor Personal Property

The tax credits do not fall within the definition of property which is taxable for *ad valorem* tax purposes. As this Court discussed in *Ohio Cellular RSA Ltd. Partnership v. Board of Public Works of State of W. Va.*, 198 W. Va. 416, 481 S.E.2d 722 (1996), the Constitution of West Virginia only provides for two types of property to be taxed in proportion to their value: real and personal²⁹. The Court defined “real property” as “[l]and, and generally whatever is erected or growing upon or affixed to land”, citing Black's Law Dictionary 1218 (6th ed.1990). *Ohio Cellular RSA Ltd. Partnership v. Board of Public Works of State of W. Va.*, 198 W. Va. at 421, 481 S.E.2d at 727. In *Ohio Cellular*, the Court held that an FCC license did not constitute real property.

This definition agrees with the Tax Commissioner’s legislative rules on the valuation of commercial and industrial real property, which, in section 110 W. Va. C.S.R. § 1P-2, address the valuation of the land itself, together with “improvements to the land” and “improvements on the land”. 110 W. Va. C.S.R. § 1P-2.1.2.1 defines improvements to the land as “land

²⁹ W. Va. Const. art. X, § 1 provides, in pertinent part: “Subject to the exceptions in this section contained, taxation shall be equal and uniform throughout the State, and all property, both real and personal, shall be taxed in proportion to its value to be ascertained as directed by law.”

improvements, the value of which are included in the value of land” and gives examples, including “privately owned drainage systems, driveways, walks, etc”. 110 W. Va. C.S.R. § 1P-2.1.2.2 defines improvements on the land as “buildings and structures” that are “valued separate and apart from the land”. Unless something is land, a tangible improvement to the land, or a building or a structure, it cannot be considered to be real property in West Virginia. Tax credits fit none of these criteria and simply cannot be assessed as a part of the value of real property.

The Court in *Ohio Cellular* also held that W. Va. Code § 11-5-3 defines “personal property” for tax purposes as follows:

The words ‘personal property,’ as used in this chapter, shall include all fixtures attached to land, if not included in the valuation of such land entered in the proper land book; all things of value, moveable and tangible, which are the subjects of ownership; all chattels, real and personal; all notes, bonds, and accounts receivable, stocks and other intangible property.

Clearly, a tax credit is not a “fixture attached to the land”, nor is it “moveable and tangible”; accordingly, it fits within neither of the first two categories of personal property, just as was true of the FCC license in *Ohio Cellular*.

The Assessors of Kanawha County and Mason County consider the tax credit to be a chattel real. See *Guidelines for the Appraisal for Ad Valorem Tax Purposes of Low Income Housing Tax Credit Properties Kanawha County, West Virginia* (2004) at 5. Kanawha County, however, offers no support for this conclusion. In *Ohio Cellular*, the Court defined a “chattel real” as “[s]uch as concern real property, such as leasehold estates; interests issuing out of, or annexed to, real estate;.... An interest in real estate less than a freehold or fee”, citing Black's Law Dictionary 236 (6th ed.1990). *Ohio Cellular, supra*, 198 W.Va. at 421, 481 S.E.2d at 727. It also referenced 63A Am.Jur.2d Property § 23 (“Chattels real are interests in real estate less than freehold ... [and] are to be distinguished, on the one hand, from things which have no

concern with the land, such as mere movables and rights connected with them, which are chattels personal, and on the other hand, from a freehold, which is realty” (footnotes omitted)), *id.*, and cited *Blair v. Freeburn Coal Corp.*, 163 W.Va. 23, 253 S.E.2d 547 (1979), in which the Court held that a coal tittle was a chattel real because “it is an interest in the real estate less than a freehold”. *Id.*, 163 W.Va. at 30, 253 S.E.2d at 552. Since an FCC license does not concern real property; the Court held that it was not a chattel real. The Assessor of Mason County considered the tax credit to be an interest “issuing out of, or annexed to, real estate”, but it is clear that the tax credits are not an interest in the land in the sense of being an estate less than a freehold. Therefore, the tax credits, being neither real nor personal property, do not fall within the definition of property which is taxable for *ad valorem* tax purposes.

5. The Taxpayers Do Not Own the Tax Credits

As the taxpayers argued below (See Finding of Fact No. 28, Order Granting Summary Judgment at 8), the value of the tax credits should not be included in the appraised value of the properties in question for a very simple reason: *the tax credits are not owned by the limited partnerships that own the properties subject to taxation*. Rather, the tax credits are owned by the individual investors, and can only be used individually by those investors.

In West Virginia, property taxes are imposed on the *owners* of the property. W. Va. Code § 11-3-1 provides, in part: “[t]he taxes upon all property shall be paid by those *who are the owners thereof* on that day, whether assessed to them or to others” (emphasis added). 110 W. Va. C.S.R. § 1P-2.1.1.7 requires the appraisal to consider only the value of the property *to its owner* (emphasis added). Also, the Supreme Court has held that “it is the duty *of the owner* of land to have his land entered on the land books of the appropriate county, to have himself charged with the taxes due on such land, and to pay such taxes; and land which for any five

successive years shall not have been so entered and charged shall, by operation of law, be forfeited to the State”. *Backus v. Abbot*, 136 W.Va. 891, 896-897, 69 S.E.2d 48, 51-52 (1952) (emphasis added).

Here, Parkview LP, Hamlets LP, and Pine Haven LP, the Appellees herein, own the real property in question. Tr. 59-60 (Mr. Ellis explaining that the properties are owned by the limited partnerships, not the Housing Development Authority). In order to raise the funds for the land and improvements, the Appellees here sold tax credits to the individual investors in exchange for their investment in the project. Tr. 57-61. The investors now own the tax credits and may use them over a ten year period to offset their own federal income tax liabilities; the Appellees are not entitled to use the tax credits to reduce or eliminate their own tax liabilities. Tr. 59.

(Commissioners Bias and Cartmill confirming this fact). As the Court recognized in *Cottonwood Affordable Housing v. Yavapai County*, 205 Ariz. 427, 72 P.3d 357 (2003):

These tax credits are not an integral part of the real estate. They do not add to the value of the property as their use is limited to ten years and the project will continue for a minimum of fifteen years³⁰. *Any value the credits may have is to the owner and not the property.*

Id., 205 Ariz. at 429, 72 P.3d at 359 (emphasis added).

The Tax Commissioner’s rules require the appraiser to consider the value of such property *to its owner*; 110 W. Va. C.S.R. § 1P-2.1.1.7; in this case, the owner is subject to the restrictions but gains nothing from the tax credits. The Assessor of Mason County, by letter dated February 18, 2008 (Attached as Exhibit A), issued a ruling consistent with this rule that “[a]s the developer typically sells the tax credits to an investor, if such sale occurs, the investor [not the limited partnership] should be assessed for the ownership interest in the tax credits”. While the Appellees disagree that the tax credits are taxable at all, for one county to treat the tax

³⁰ Here, the restrictions continue for 30 and 40 years. See above.

credits taxable as part of the real property and another to treat them taxable to the individual investors violates the constitutional principle of equal and uniform taxation. W. Va. Const. Art. X, § 1.

It is also important to realize that “income tax consequences may vary drastically from person to person while *ad valorem* taxes are assessed *in rem*. It is a well-accepted rule of valuation that the individual personalities and opportunities of particular owners must be ignored. *Joseph Hydro Associates, Inc. v. Department of Revenue*, 1986 WL 15525 at *4, 10 Or. Tax 277 (Or.Tax, 1986). While the investors undoubtedly purchase the tax credits with the anticipation of being able to use them, uncertainty in their own financial affairs could frustrate their plans. Moreover, if these developments fail and are converted to market based housing, unclaimed tax credits are forfeited, and the investors are subject to the IRS reclaiming the credits if this occurs or if the restrictions on the developments are not honored.³¹ What value the tax credits have is speculative and depends of the circumstances of each investor, and valuing them as a part of the real property would thus violate the constitutional principle of equal and uniform taxation. See *Penna, supra*, at 62. Thus, even if this Court were to hold that the tax credits are either real or personal property and are not intangible, and thus are taxable, they are not taxable to the Appellees herein, for the simple reason that the tax credits are not owned by them.³²

³¹ The value of the tax credits also depends on the tax bracket that the investor is in, and is partially offset by the fact that, in order to invest in the project, he has foregone other investments that are far more likely to yield a market-based rate of return. The LIHTC project itself, by contrast, in all likelihood will yield little, if any return to the investor. See *McNeely, supra*, at 331. Accordingly, it is speculative at best to attempt to value the tax credits from the perspective of the investor, and again, any value the tax credits may have to him is an intangible asset and that is not subject to *ad valorem* taxation in West Virginia.

³² Treating the tax credits as separately taxable to the investors who own them is analogous to the treatment of severed mineral rights; after severance, the surface owner no longer liable for all taxes; rather, he pays only on the value of the surface (leased fee), and the owner of the mineral rights pays on the value of those rights (leasehold). See also *Great A & P Tea Co., Inc. v. Davis*, 167 W.Va. 53, 278 S.E.2d 352 (1981), holding that case a leasehold can have separate value from freehold.

6. The Assessor Failed to Establish the Value of the Tax Credits

When examining the value of the tax credits, it is critical to understand that their value, like the element of value attributed to “new” automobiles, dissipates much more rapidly than does the value of the real property since they are expended within a ten year period. Tax credits that will be worth, for example, \$1 million over a 10 year period to the investors that purchase them can only be sold by the developer to the developer for perhaps sixty cents on the dollar, due to (1) the time value of money, and (2) the fact that there is significant risk in the projects as described above in the introduction. See generally McClure, *The Low-Income Housing Tax Credit as an Aid to Housing Finance: How Well Has It Worked?*, 11 Housing Policy Debate 91(2000) at 104. In a sense, they are similar to an annuity, which could be purchased today and which would guarantee a sum certain annually for the next ten years. Seen in this light, it is clear that the tax credits should be treated as an intangible asset, as would the annuity.³³

Even in the cases in which the courts held that the value of the tax credits should be included in the value of the property, it is clear that the assessing authority determined the *present value* of the tax credits after considering that the credits sell for a fraction of their apparent value and after determining how much, if any, of the tax credits remain to be claimed. See, for example, *Huron Ridge LP v. Ypsilanti Tp.*, *supra* (in which the parties agreed that “the most applicable method within the income approach is a discounted cash flow analysis in which the combined cash flows from operation of the subject property and the unallocated (remaining) [tax credits] are discounted to a present value as of each date of valuation.”); *Rainbow Apartments v. Illinois Property Tax Appeal Bd.*, 326 Ill.App.3d 1105, 762 N.E.2d 534 (Ill.App. 4

³³ The tax credits, however, incorporate more risk, due to the possibility that the project could fail and due to the fact that they can be reclaimed in the event the project fails to adhere to the use restrictions, and that risk adversely affects their present value.

Dist., 2001) (the appraiser calculated the *present value* of the tax credits); *Spring Hill, L.P. v. Tennessee State Bd. of Equalization*, 2003 WL 23099679 at *3 n.11 (Tenn.Ct.App., 2003) (same; “Mr. Davis conducted a *discounted cash flow analysis* to determine the effect of the tax credit on the value of the each property in dispute); *Town Square Ltd. Partnership v. Clay County Bd. of Equalization*, *supra* (noting that, in some instances, appraisers will use the *present value* of the tax credits in valuing the property.); and *Hometowne Associates*, *supra* (noting that valuing the tax credits requires determining the amount of the federal income tax credits *still available for use* by the investors and in which the amount of economic obsolescence claimed in the taxpayer’s first alternative was reduced by the *discounted value* of the remaining tax credits in the calculation of its second alternative).

Here, the Assessor introduced no evidence as to how much, if any, of the tax credits remained to be taken by the investors or of over what period those tax credits could be claimed, no evidence of the value actually received by the limited partnerships from the sale of the tax credits, and no evidence that the tax credits were properly valued by a generally accepted appraisal practices such as a discounted cash flow analysis to determine their present value. Thus, even if the Appellants are correct that the value of the tax credits should be included, they failed to demonstrate what that value was. Under these circumstances, the Court below was entirely correct to hold that “the Petitioners correctly point out that their argument here cannot succeed, because there is no evidence in the record as to what value the Respondents place on these tax credits”, Conclusion of Law No. 13, Order Granting Summary Judgment at 12 (in part, footnote omitted).

7. The Assessor Simply Failed to Rebut the Taxpayers' Showing that the Assessments Were Excessive

Neither the Tax Commissioner nor the Assessor her claim that the income approach is inapplicable to valuing these properties; quite to the contrary, the Assessor used that approach here, purportedly at the Tax Commissioner's behest, and the Tax Commissioner's appraiser used the income approach in the companion cases. The Tax Commissioner further concedes that the restricted rents should be used when using the income approach. Therefore, the Court below was fully justified in its conclusion that "[t]he Petitioners have demonstrated that the income approach is the most appropriate method for Low Income Housing Tax Credit properties, and that the use of the actual, restricted rents, that are locked in place for 30 years, are more appropriate to use than market based rent." Conclusion of Law No. 15 (in part), Order Granting Summary Judgment at 12. Since the Appellees' income approach calculations were properly performed, and since their results were much lower than the Assessor's result by the cost approach, the Appellees met their burden to show that the assessments were excessive. By contrast, the Appellants simply failed to carry their burden of production.³⁴

As demonstrated above, the differences in values between the Assessor's cost approach and the taxpayers' income approach are attributable both to the value of the tax credits and to functional obsolescence caused by the superadequacies of construction required by governmental

³⁴ The taxpayers have the burden of persuasion throughout the hearing before the Board, and that burden never shifts to the taxing authority. *See Foster, supra*. The burden of production, however, shifts as described in *Pocahontas Land, supra*. *See Foster*, 672 S.E.2d at 165, quoting *Mayhew v. Mayhew*, 205 W.Va. 490, 497 n. 15, 519 S.E.2d 188, 195 n. 15 (1999):

[a]s a general matter, the burden of proof consists of two components: burden of production and bur-den of persuasion. The burden of persuasion re-quires the party upon whom it is placed, to convince the trier of fact ... on a given issue. When a party has the burden of persuasion on an issue, that burden does not shift. The burden of production merely requires a party to present some evidence to rebut evidence proffered by the party having the burden of persuasion.

regulations and to economic obsolescence resulting from the rent restrictions. As to the two forms of obsolescence, there is no question that both types are present in this case, but there is no evidence in the record that the Assessor made the appropriate allowance for either in his cost approach calculation.

The tax credits are intangible, rather than real or personal property, and thus are not taxable in West Virginia. Moreover, even if they were taxable, they are not owned by the limited partnerships that own the real estate, and are not taxable to them. In this case, the Circuit Court correctly concluded that “[w]hile it is true that ‘the general rule is that valuation for taxation purposes fixed by an assessing officer are presumed to be correct’, the Assessor has a duty to prove that his appraisals are correct when presented with evidence to the contrary. *In re Tax Assessments Against Pocahontas Land Co.*, 172 W.Va. 53 at 61, 303 S.E.2d 691 at 699 (1983).” Conclusion of Law No. 16 (in part), Order Granting Summary Judgment at 12.

Therefore, even if the value of the tax credits should have been included in the value of the real estate, the Court below correctly concluded that “[t]he Respondents continually fall back on the position that ‘the general rule is that valuation for taxation purposes fixed by an assessing officer are presumed to be correct’, yet they offer no concrete evidence in this record showing how the Assessor accounted for the tax credits and what value was placed on them”. Conclusion of Law No. 14, Order Granting Summary Judgment at 12 (footnote omitted). Thus, the Court below properly held that “[g]iven the facts in this case, one cannot say that the Assessor’s valuation is supported by substantial evidence”. Conclusion of Law No. 16 (in part), Order Granting Summary Judgment at 12.

Under these circumstances, then, the Court below had no choice but to find that “[t]he Cabell County Commission sitting as the Board of Equalization and Review on February 19th

and February 22nd, 2008, was clearly wrong in review of the reliable probative and substantial evidence on the record, and that its decision was arbitrary and abuse of discretion which was clearly unwarranted under these circumstances.” See Conclusion of Law No. 18, Order Granting Summary Judgment at 13.

F. The Flaws in the Assessor’s Income Approach Confirm that His Cost Approach Result is Excessive

At the second hearing before the Board on February 22, the Assessor’s representative informed the Board that he had been instructed by the State Tax Legal Department that the Assessor could use the income approach as a “check” on their appraised value, but that if the Assessor used the income approach in this fashion, he must use median market rents in that approach. Tr. 55³⁵. The following table shows that, in every case, the result of the Assessor’s income approach was higher than his final appraised values as determined with the cost approach:

Property	Assessor’s Appraised Values	Assessor’s Income Approach
The Parks	\$2,952,100	\$3,150,000
The Hamlets	\$3,015,000	\$3,150,000
Pine Haven	\$2,017,000	\$2,070,000

The use of market-based as opposed to actual, restricted rents does not fully explain the differences between the results of the Assessor’s income approach and that performed by the Appellees’ appraiser Mr. Bunch. The Assessor also used a different occupancy rate and capitalization rate³⁶, and his estimated expenses are far lower than the actual expenses itemized

³⁵ The instructions to the Assessor here, then, are at odds with the position taken by the Tax Commissioner in the companion cases, where, as explained above, the Tax Commissioner urges this Court to rule that the restricted rents should be used in the income approach.

³⁶ There is no evidence in the record that the Assessor’s capitalization rate was derived, as required, “from current available market data by dividing annual net income by the current selling price of comparable properties.” 110 W. Va. C.S.R. § 1P-2.2.1.2.

in Mr. Bunch's appraisals. The differences between the income approaches performed by the Assessor and the Appellees' appraiser are summarized in the following table³⁷.

	The Parks		The Hamlets		Pine Haven	
	Assessor	Appraiser	Assessor	Appraiser	Assessor	Appraiser
Gross Income	\$420,000	\$284,856	\$420,000	\$291,276	\$276,000	\$192,600
Occupancy Rate	90%	95%	90%	95%	90%	95%
Estimated Rent	\$378,000	\$270,613	\$378,000	\$276,712	\$248,400	\$182,970
Expense Rate	25%	67%	25%	62%	25%	68%
Expenses	\$94,500	\$182,149	\$94,500	\$172,144	\$62,100	\$123,992
Net Income	\$283,500	\$88,463	\$283,500	\$104,568	\$186,300	\$58,978
Cap Rate	9%	11.6195%	9%	11.6195%	9%	11.6195%
Appraised Value	\$3,150,000	\$750,000	\$3,150,000	\$900,000	\$2,070,000	\$500,000

In fact, except for the occupancy rate (which makes very little difference), in every case, the different values used by the Assessor caused his income approach value to increase substantially. For example, the Assessor used an expense rate of 25% the estimated gross rent after allowance for vacancies, whereas the appraisals list *actual* expenses which total almost three times as much. Even if the 25% figure is appropriate for commercial apartments, according to Rosenblum, "expenses are higher for LIHTC owners because they must meet certain reporting, record keeping and documentation edicts beyond conventional practice." Rosenblum at 37. Mr. Childers testified that "the management agents and the owners spend an inordinate amount of money back into the project to make sure that they remain affordable and remain decent, safe housing for low income families". Tr. 21-22. 110 W. Va. C.S.R. § 1P-2.1.1.9 requires the appraisal to consider "the income, if any, which the property *actually produces* and has produced within the next preceding three (3) years" (emphasis added). Clearly, the Assessor should have used the actual expenses, rather than his artificially low rule of thumb.

³⁷ Source of data: the Assessor's data comes from the exhibits he introduced and Mr. Perry's testimony in the Transcript at page 56. The Appraisal data comes from each appraisal introduced into evidence. Note that the Appraised Value = Net Income / Cap Rate, so a lower cap rate will increase the appraised value.

Had the Assessor used the same values as did the Appellees' appraiser for everything except rent, the result of his income approach calculations would have resulted in a value substantially lower than his original appraised value by the cost approach.³⁸ Mr. Perry's testimony indicates that, according to the State Tax Department, the Assessor would still have been required to use his original cost approach value. Tr. 55 ("we can use a market rent [income] approach as a check"); Tr. 57 ("we're just using [the income approach] as a check").

The Tax Department's purported instructions are contrary to 110 W. Va. C.S.R. § 1P-2.2.2, which requires the Assessor to correlated the results of his income and cost approaches to determine the final value. Had the income approach been properly performed, this correlation been performed, the appraised values of Appellees' properties would at least have been substantially reduced, even had the Assessor failed to properly perform the cost approach.

The Court below was justified in its conclusion that "[t]he fact that the Respondents performed their own income approach appraisal as a check on their cost approach demonstrates that they understand that the income approach is likely the best way to value the property." Conclusion of Law No. 11, Order Granting Summary Judgment at 11. At the very least, the Assessor's use of the income approach takes this dispute out of the realm of a simple dispute over which valuation method is better.

It is remarkable also that the position the Tax Commissioner took in the case is diametrically opposed to that he took before the Boards of Equalization and Review in *Heathermoor* and *Stone Brooke* cases now before this Court. There, the Tax Commissioner used the income approach to value the two LIHTC properties. Here, however, according to the

³⁸ If the only difference had been the use of market rather than actual rents, the Assessor's appraised value of The Parks would have been about \$1,870,000, rather than \$3,150,000. The Assessor's appraised value of The Hamlets would have been about \$1,950,000 rather than \$3,150,000, and would have been about \$1,190,000 for Pine Haven, rather than \$2,070,000.

Assessor's testimony, the Tax Commissioner instructed the Assessor to use the cost approach. While the Assessor was permitted to use the income approach "as a check", he was specifically told he could not use the results of the income approach as the basis for his appraised value. As noted above, this disparate treatment of similarly situated taxpayers cannot achieve the constitutionally required equal and uniform taxation. W. Va. Const. Art. X, § 1.

V. Conclusion

In this case, the Assessor valued the properties in question by the cost approach, against the great weight of authority that holds that the cost approach cannot be used to value LIHTC properties because the rent restrictions would make an investment of this magnitude untenable. In doing so, the Assessor failed to attribute either functional or economic obsolescence to the property, in contravention of both generally accepted appraisal practices and the Tax Commissioner's legislative rules.

By contrast, the independent professional appraiser properly used the income approach to value the Appellees' properties, and in that approach properly used the actual restricted rents in determining the net income to capitalize, both in accordance with generally accepted appraisal practices.

The Assessor also performed an income approach, but he used artificial "market" rents that were much higher than the restricted rents that the Appellees (or any subsequent purchasers of these properties) actually receive. He also used an assumed level of expenses for these properties that were only about a third of the actual expenses presented in the appraisals, and an unrealistically low capitalization rate. Individually, any of these differences would artificially inflate the result of the Assessor's calculation, but it required the *combination of all three of*

these differences to yield a result from the Assessor's income approach that was similar to that of his cost approach.

The fact that the Assessor had to use unattainable market rents, artificially low expenses, and an artificially low capitalization rate to confirm the results of his cost approach is a clear indication that the results of his cost approach are far too high. The results of his cost approach are too high, in part, because they include the value of the tax credits. The tax credits, however, aren't owned by the limited partnerships that are the owners of these properties and have no benefit to them. Even if they were, they are intangible property and do not constitute real or personal property subject to taxation in West Virginia.

The Appellees here met their burden of proof by the introduction of fee appraisals performed by a qualified appraiser, performed in accordance with generally accepted appraisal practices, and by the appraiser's testimony. The Assessor, by contrast, did not meet his burden of proof to support his appraisals which, contrary to generally accepted appraisal practices, were based on the cost approach. His cost approach results can only be explained by the recognition that they include the value of the tax credits, which are non-taxable property that is not owned by the limited partnerships that own the properties here in question, and by his failure to deduct an appropriate amount for economic obsolescence. Thus, the only competent evidence in the record was that contained in the appraisals submitted by the Appellees' appraiser, and it was plain error for the Board to decide to uphold the Assessor's values.

It is not necessary for this Court to decide which valuation approach should be used for LIHTC properties. Rather, in the absence of legislative rules on this subject promulgated by the Tax Commissioner, this Court should enunciate similar general principles to those set by the Supreme Court of Ohio in *Woda Ivy Glen*, *supra* to guide the various Assessors in the future:

1. Low Income Housing Tax Credits are an intangible asset that is neither real nor personal property, and they cannot be viewed as pertaining to the realty.
2. Both functional obsolescence (in the form of the superadequacies required by federal law) and economic obsolescence (in the form of the restrictions on the properties use and on the rents that can be charged) affect the value of LIHTC projects.
3. In the context of appraising real property for tax purposes, the use restrictions imposed on LIHTC properties constitute governmental restrictions for the general welfare that must be taken into account when determining the value of these properties.

Under these general principles, both the cost approach and the income approach can be expected to yield an accurate value for this type of property.

Both the Tax Commissioner and the Assessor here assert that the Assessor has the discretion to select which of the methods of appraisal to use, and since the cost approach is one of the three methods contemplated by the Tax Commissioner's legislative regulations, the Assessor could not have abused his discretion.³⁹ The Tax Commissioner, in his brief, offers no legal or generally accepted appraisal authority to justify his selection of the cost approach; he seems quite confident that his "because I said so" justification will be enough to support his contention that the Assessor's decision to use the cost approach is entitled to deference.

Yet so too is the income approach one of the three methods approved by the Tax Commissioner's legislative regulations, and the great weight from other jurisdictions indicates that the income approach is the approach most suited to valuing LIHTC properties and that restricted rents should be used in that approach. Since the taxpayer's income approach values

³⁹ The Tax Commissioner makes an even more ludicrous argument that "[n]either apartment complex has challenged the accuracy of the Assessors' valuations. Therefore, the cost calculations must be mathematically correct." Obviously, the former statement is incorrect, as the taxpayers have challenged their assessments in the manner prescribed by W. Va. Code § 11-3-25. And as discussed above, the Assessor's cost approach calculations are incorrect in that (1) they improperly include the value of the tax credits, and (2) the Assessor's failed to make the appropriate deductions for functional and economic obsolescence.

were markedly lower than the Assessor's cost approach calculations, something was very clearly wrong. West Virginia is a "true and actual" value state, which means that property is only worth what a willing buyer and seller will pay for it in an arms' length transaction. Here, no investor would pay the full cost to construct these apartments, because the rent restrictions that remain in place for 30 or 40 years simply cannot support the required investment. Nor would any investor agree to purchase these apartments for the price indicated by the Assessor's cost approach subject to these restrictions. The assessed value, then, is far in excess of the "true and actual" value of the real property.

If the only judicial review applied to the propriety of an appraisal is to determine if the Tax Commissioner employed an approach to valuation contained in a legislative rule, the result is to encourage inaccurate, but not necessarily higher, appraisals. The effective absence of judicial review does not preserve the tax base. Rather, the effective absence of judicial review inevitably leads to the deterioration of the appraisals performed by the Tax Commissioner and threatens to return the state to the property tax crises of 1904, 1931, 1957 and 1982. The tax Commissioner must be able to defend the accuracy of his appraisals. Certainly he is entitled to a presumption in favor of correctness. He is not entitled to an irrefutable presumption that whatever appraisal he produces accurately reflects the true and actual value of a particular property. The absence of effective judicial review effectively creates such an irrefutable presumption.

VI. Prayer for Relief

WHEREFORE,

Parkview LP PRAYS this honorable Court to affirm the decision on the Circuit Court of Cabell County reducing the value of its real property in Cabell County for tax year 2008 from \$2,952,100 to \$750,000;

Hamlets LP PRAYS this honorable Court to affirm the decision on the Circuit Court of Cabell County reducing the value of its real property in Cabell County for tax year 2008 from \$3,015,000 to \$900,000;

Pine Haven LP PRAYS this honorable Court to affirm the decision on the Circuit Court of Cabell County reducing the value of its real property in Cabell County for tax year 2008 from \$2,017,000 to \$500,000; and

all PRAY for such other relief as may be appropriate..

Respectfully Submitted,

PARKVIEW LP,
THE HAMLETS LP
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By Counsel



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